Wraps and Platforms – operating principles and practical issues

Using Behavioural Finance to Guide Wealth Management

Daniel Egan
Behavioural Finance, Barclays Wealth

BARCLAYS WEALTH

Building upon two views of investing

Harry Markowitz – Nobel Prize 1990

Daniel Kahneman – Nobel Prize 2002

7

BARCLAYS WEALTH

Wraps and Platforms – operating principles and practical issues

Assisting private clients requires a distinct set of tools

Private clients:

- may not be able to define their expectations clearly
- may be more susceptible to emotional reactions in their investment decisions
- will have different financial beliefs that determine the appropriate investment goals and investment styles
- Like a bespoke tailor recognises each person is different, Barclays Wealth focuses on recognising that each client is different

8 BARCLAYS WEALTH

Attitudes to investing are multi-dimensional

"I want my banker to run my money in the same way as I run my business. I like taking risks, I don't have much time and I want access to the most advanced and innovative products and investment idea"
– **The Entrepreneur**

"I need sophisticated cash management services, coupled with advanced insurance products. My preference is to invest in financial assets that are real and appear easy to understand, such as residential property"
– **The Professional Sports Player**

"I don't really believe in the skills of investment managers. My main objective is to preserve my inherited wealth and it is paramount that I understand what is happening with my investments"
– **The Wealth Inheritor**

9 BARCLAYS WEALTH

Wraps and Platforms – operating principles and practical issues

Traditional industry risk tolerance measures

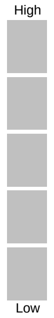
- Represents risk attitude as a single dimension
- Not behaviourally designed or statistically robust
- Often more a test of financial knowledge or numeracy than risk tolerance
- Mask true story by reducing distinct aspects to a single number

Example: Two Different Individuals

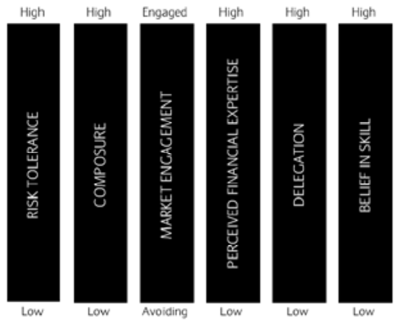
	Client 1	Client 2
Psychological Risk Tolerance		
Investment Horizon		
Profiling Output		

The result is behavioural profiling considerably beyond the industry standard

Traditional One-Dimensional Approach
Risk Tolerance Questionnaire



Barclays Wealth Behavioural Approach
Financial Personality Discovery



You are not one-dimensional, all aspects of your personality matter

Wraps and Platforms – operating principles and practical issues

Financial objectives are a mix of financial psychology, investment objectives and risk capacity

Financial Personality	Investment Objectives	Risk Capacity
Risk Tolerance	Time Horizon Profile	Total Wealth
Composure	Income Requirements	Proportion of Wealth Under Consideration
Market Engagement	Liquidity Profile	Stability of Existing Asset Portfolio
Perceived Financial Expertise	Personal Inflation Rate	Years of Future Earnings
Delegation	Tax Optimisation	Stability of Future Earnings
Belief in Skill		

12

BARCLAYS WEALTH

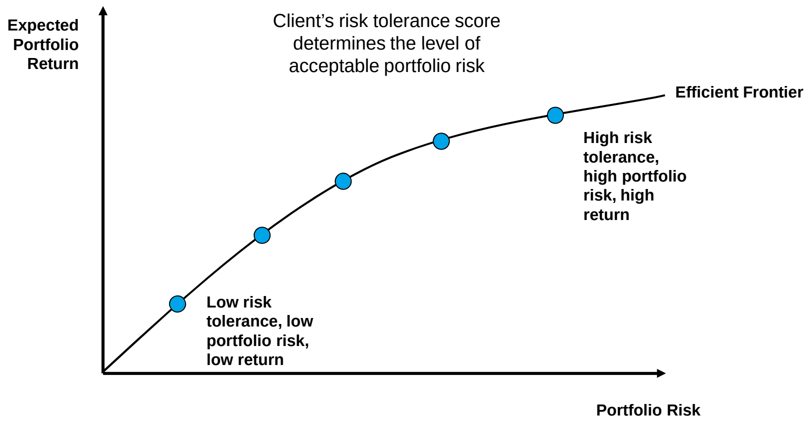
Tailoring the investment journey

13

BARCLAYS WEALTH

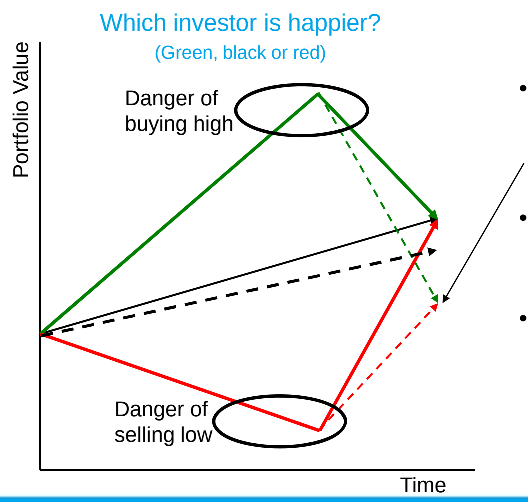
Wraps and Platforms – operating principles and practical issues

Mapping the highest return, risk-appropriate portfolio



14 BARCLAYS WEALTH

The emotional experience with the investment journey has potentially greater influence on the final result



- Volatile paths may cause short term knee-jerk decisions … resulting in worse performance
- Absolute returns investment strategies help provide smooth investment paths
- Smoothing leads to emotional comfort, self-control and long term performance

15 BARCLAYS WEALTH

Wraps and Platforms – operating principles and practical issues

Mental accounting matters – cash in gains, ride losses

Situation A

- A month ago you bought a stock which you believed was undervalued by 30%. Today it is up 20% from that point. Nothing has changed your estimate of its fair market price, so you now believe its fair market price is undervalued by 10%.
- How likely are you to sell?

Very Likely: 34%

Situation B

- A month ago you bought a stock which you believed was undervalued by 30%. Today it is down 20% from that point. You now believe its fair market price is undervalued by 10%.
- How likely are you to sell?

Very Likely: 5%

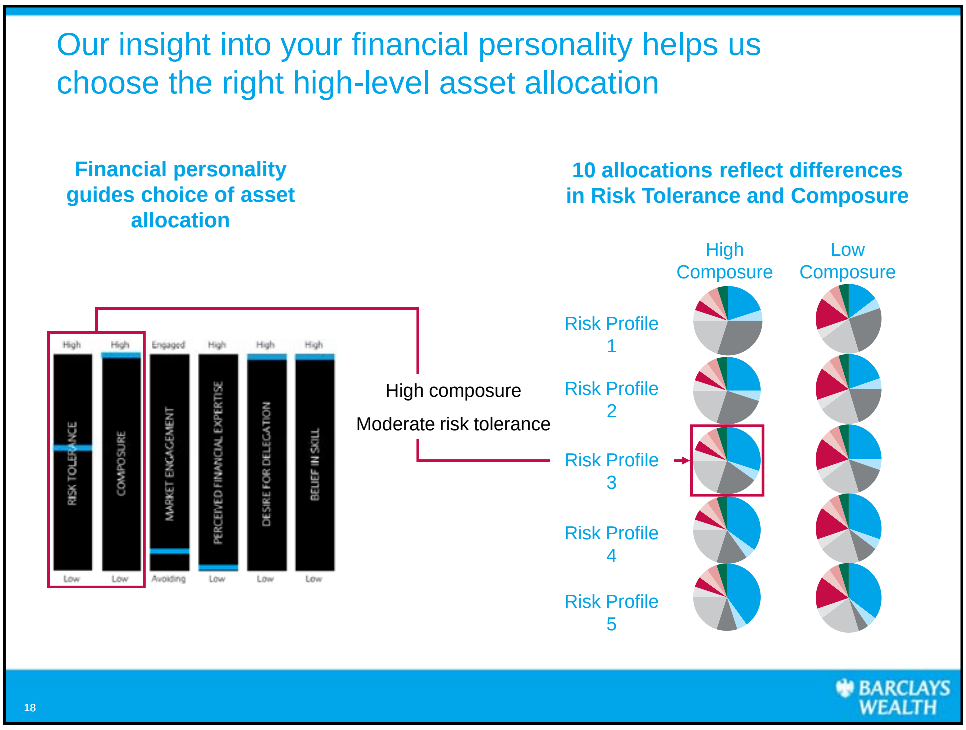
Source: BWA IR workshop responses

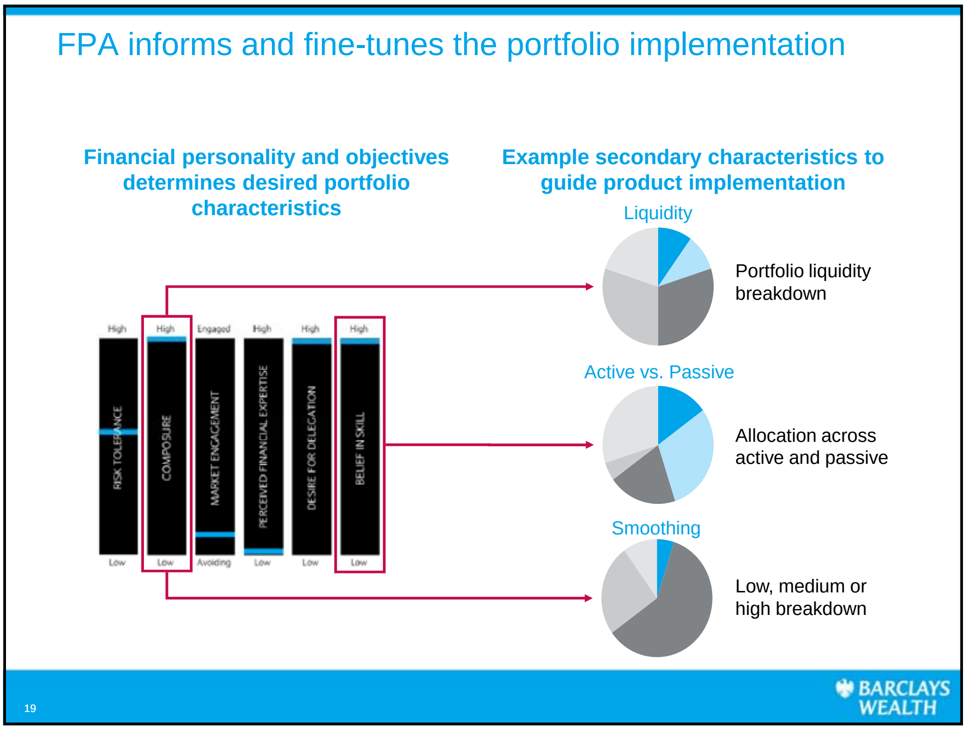
16 BARCLAYS WEALTH

Focus on the past, miss the future

17 BARCLAYS WEALTH

Wraps and Platforms – operating principles and practical issues





Wraps and Platforms – operating principles and practical issues

The new frontier of Wealth Management

20

BARCLAYS WEALTH